

**REPORT OF THE AUDIT OF THE  
LEE COUNTY  
SHERIFF**

**For The Year Ended  
December 31, 2005**

## CONTENTS

PAGE

INDEPENDENT AUDITORS' REPORT .....	1
STATEMENT OF REVENUES, EXPENDITURES, AND EXCESS FEES - REGULATORY BASIS .....	3
NOTES TO FINANCIAL STATEMENT.....	6
COMMENTS AND RECOMMENDATIONS.....	8
REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF THE FINANCIAL STATEMENT PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS .....	11

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The Honorable L.C. Reese, Lee County Judge/Executive  
Honorable Harvey Pelfrey, Lee County Sheriff  
Members of the Lee County Fiscal Court

Independent Auditors' Report

We have audited the accompanying statement of revenues, expenditures, and excess fees - regulatory basis of the County Sheriff of Lee County, Kentucky, for the year ended December 31, 2005. This financial statement is the responsibility of the County Sheriff. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, and the Audit Guide for County Fee Officials issued by the Auditor of Public Accounts, Commonwealth of Kentucky. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, the County Sheriff's office prepares the financial statement on a regulatory basis of accounting that demonstrates compliance with the laws of Kentucky, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statement referred to above presents fairly, in all material respects, the revenues, expenditures, and excess fees of the County Sheriff for the year ended December 31, 2005, in conformity with the regulatory basis of accounting.

The Honorable L.C. Reese, Lee County Judge/Executive  
Honorable Harvey Pelfrey, Lee County Sheriff  
Members of the Lee County Fiscal Court


In accordance with Government Auditing Standards, we have also issued our report dated August 4, 2006, on our consideration of the County Sheriff's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Based on the results of our audit, we have presented the accompanying comments and recommendations, included herein, which discusses the following report comments:

- The Sheriff Should Require The Depository Institution To Pledge Or Provide Sufficient Collateral And Enter Into A Written Agreement To Protect Deposits
- The Fiscal Court Should Set The Deputies And Assistants Salary Limit
- The Sheriff's Office Lacks Adequate Segregation Of Duties

This report is intended solely for the information and use of the County Sheriff and Fiscal Court of Lee County, Kentucky, and the Commonwealth of Kentucky and is not intended to be and should not be used by anyone other than these interested parties.

Respectfully submitted,

A handwritten signature in black ink that reads "Morgan-Franklin, LLC". The signature is written in a cursive, flowing style.

Morgan-Franklin, LLC

Audit fieldwork completed-  
August 4, 2006

LEE COUNTY  
HARVEY PELFREY, COUNTY SHERIFF  
STATEMENT OF REVENUES, EXPENDITURES, AND EXCESS FEES - REGULATORY BASIS

For The Year Ended December 31, 2005

Revenues

State - Kentucky Law Enforcement Foundation Program Fund	\$	1,681
State Fees For Services:		
Cabinet For Human Resources	\$	360
HB 413		1,681
Excise Tax		3,461
Election Commission		880
Waiting On Court		9,955
Sheriff Security Service		2,497
		18,834
Circuit Court Clerk:		
Fines and Fees Collected		580
County Clerk - Delinquent Taxes		1,427
Commission On Taxes Collected		74,778
Fees Collected For Services:		
Auto Inspections		1,097
Accident and Police Reports		194
Serving Papers		6,650
Carrying Concealed Deadly Weapon Permits		2,940
10% Add On Fees		9,059
		19,940
Other:		
Miscellaneous		2,211
Jail Diversion/Transportation		2,028
		4,239
Interest Earned		542
Borrowed Money:		
State Advancement		24,000
Transfer From Tax Account		2,000
		26,000
Total Revenues	\$	148,021

The accompanying notes are an integral part of this financial statement.

## LEE COUNTY

HARVEY PELFREY, COUNTY SHERIFF

## STATEMENT OF REVENUES, EXPENDITURES, AND EXCESS FEES - REGULATORY BASIS

For The Year Ended December 31, 2005

(Continued)

Expenditures

## Operating Expenditures and Capital Outlay:

## Personnel Services-

Deputies' Salaries	\$ 18,758
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## Contracted Services-

Advertising	714
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## Materials and Supplies-

Office Materials and Supplies	1,127
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Uniforms	2,112
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## Auto Expense-

Gasoline	19,999
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Maintenance and Repairs	5,059
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## Other Charges-

Conventions and Travel	529
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Dues	300
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Postage	187
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Bond	808
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Carrying Concealed Deadly Weapon Permits	2,345
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Miscellaneous	1,354
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## Capital Outlay-

Office Equipment	3,186
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## Debt Service:

State Advancement	24,000
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Transfer To Tax Account	2,000
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## Total Expenditures

\$ 82,478
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The accompanying notes are an integral part of this financial statement.

LEE COUNTY  
HARVEY PELFREY, COUNTY SHERIFF  
STATEMENT OF REVENUES, EXPENDITURES, AND EXCESS FEES - REGULATORY BASIS  
For The Year Ended December 31, 2005  
(Continued)

Net Revenues	\$ 65,543
Less: Statutory Maximum	<u>\$ 62,280</u>
Excess Fees	3,263
Less: Training Incentive Benefit	<u>3,194</u>
Excess Fees Due County for 2005	69
Payments to Fiscal Court - June 15, 2006	<u>69</u>
Balance Due Fiscal Court at Completion of Audit	<u><u>\$ 0</u></u>

The accompanying notes are an integral part of this financial statement.

LEE COUNTY  
HARVEY PELFREY, COUNTY SHERIFF  
NOTES TO FINANCIAL STATEMENT

December 31, 2005

Note 1. Summary of Significant Accounting Policies

A. Fund Accounting

A fee official uses a fund to report on the results of operations. A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

A fee official uses a fund for fees to account for activities for which the government desires periodic determination of the excess of revenues over expenditures to facilitate management control, accountability, and compliance with laws.

B. Basis of Accounting

KRS 64.820 directs the fiscal court to collect any amount, including excess fees, due from the County Sheriff as determined by the audit. KRS 134.310 requires the County Sheriff to settle excess fees with the fiscal court at the time he files his final settlement with the fiscal court.

The financial statement has been prepared on a regulatory basis of accounting, which demonstrates compliance with the laws of Kentucky and is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. Under this regulatory basis of accounting revenues and expenditures are generally recognized when cash is received or disbursed with the exception of accrual of the following items (not all-inclusive) at December 31 that may be included in the excess fees calculation:

- Interest receivable
- Collection on accounts due from others for 2005 services
- Reimbursements for 2005 activities
- Tax commissions due from December tax collections
- Payments due other governmental entities for payroll
- Payments due vendors for goods or services provided in 2005

The measurement focus of a fee official is upon excess fees. Remittance of excess fees is due to the County Treasurer in the subsequent year.

C. Cash and Investments

At the direction of the fiscal court, KRS 66.480 authorizes the County Sheriff's office to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

The accompanying notes are an integral part of this financial statement.



LEE COUNTY  
HARVEY PELFREY, COUNTY SHERIFF  
NOTES TO FINANCIAL STATEMENT  
December 31, 2005  
(Continued)

Note 2. Employee Retirement System

The county officials and employees have elected to participate in the County Employees Retirement System (CERS), pursuant to KRS 78.530 administered by the Board of Trustees of the Kentucky Retirement Systems. This is a cost-sharing, multiple-employer defined benefit pension plan that covers all eligible full-time employees and provides for retirement, disability, and death benefits to plan members.

Benefit contributions and provisions are established by statute. Nonhazardous covered employees are required to contribute 5.0 percent of their salary to the plan. The county's contribution rate for nonhazardous employees was 8.48 percent for the first six months and 10.98 percent for the last six months of the year. Hazardous covered employees are required to contribute 8 percent of their salary to the plan. The county's contribution rate for hazardous employees was 22.08 percent for the first six months and 25.01 percent for the last six months of the year.

Benefits fully vest on reaching five years of service for nonhazardous employees. Aspects of benefits for nonhazardous employees include retirement after 27 years of service or age 65. Aspects of benefits for hazardous employees include retirement after 20 years of service or age 55.

Historical trend information pertaining to CERS' progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Retirement Systems' annual financial report which is a matter of public record. This report may be obtained by writing the Kentucky Retirement Systems, 1260 Louisville Road, Frankfort, Kentucky 40601-6124, or by telephone at (502) 564-4646.

Note 3. Deposits

The Sheriff maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC) in accordance with KRS 66.480(1)(d). According to KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the Sheriff and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution.

Custodial Credit Risk – Deposits

Custodial credit risk is the risk that in the event of a depository institution's failure, the Sheriff's deposits may not be returned to it. The Sheriff does not have a deposit policy for custodial credit risk but rather follows the requirements of KRS 41.240(4). As of November 9, 2005, \$977,641 of the Sheriff's bank balance of \$1,077,641 was exposed to custodial credit risk.

- Uninsured and unsecured \$977,641

## COMMENTS AND RECOMMENDATIONS

LEE COUNTY  
HARVEY PELFREY, COUNTY SHERIFF  
COMMENTS AND RECOMMENDATIONS

For The Year Ended December 31, 2005

STATE LAWS AND REGULATIONS:

The Sheriff Should Require The Depository Institution To Pledge Or Provide Sufficient Collateral And Enter Into A Written Agreement To Protect Deposits

On November 9, 2005, \$977,641 of the Sheriff's deposits of public funds were uninsured and unsecured. According to KRS 66.480(1)(d) and KRS 41.240(4), financial institutions maintaining deposits of public funds are required to pledge securities or provide surety bonds as collateral to secure these deposits if the amounts on deposit exceed the \$100,000 amount of insurance coverage provided by the Federal Deposit Insurance Corporation (FDIC). The Sheriff should require the depository institution to pledge or provide collateral in an amount sufficient to secure deposits of public funds at all times. We also recommend the Sheriff enter into a written agreement with the depository institution to secure the Sheriff's interest in the collateral pledged or provided by the depository institution. According to federal law, 12 U.S.C.A. § 1823(e), this agreement, in order to be recognized as valid by the FDIC, should be (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution.

*Sheriff's Response: None*

The Fiscal Court Should Set The Deputies And Assistants Salary Limit

The fiscal court did not set the salary limit for the Sheriff's deputies and assistants. Per KRS 64.530, the fiscal court shall fix annually the maximum amount, including fringe benefits, which the officer may expend for deputies and assistants, and allow the officer to determine the number to be hired and the individual compensation of each deputy and assistant. We recommend the Sheriff comply with KRS 64.530 by requesting the fiscal court set the deputies and assistant salary limit.

*Sheriff's Response: None*

LEE COUNTY  
HARVEY PELFREY, COUNTY SHERIFF  
COMMENTS AND RECOMMENDATIONS  
For The Year Ended December 31, 2005  
(Continued)

INTERNAL CONTROL - REPORTABLE CONDITIONS:

The Sheriff's Office Lacks Adequate Segregation Of Duties

The Sheriff's office has a lack of segregation of duties. Due to the Entity's diversity of official operations, small size and budget restrictions, the official has limited options for establishing an adequate segregation of duties. We are recommending that the following compensating controls be implemented to offset this internal control weakness:

- The Sheriff should periodically compare daily bank deposits to daily checkout sheets and then compare the daily checkout sheets to the receipts ledgers. Any differences should be reconciled. He should document this by initialing the bank deposits, daily checkout sheets and receipts ledgers.
- The Sheriff should reconcile monthly reports to source documents and receipts and disbursements ledgers.
- The Sheriff should periodically compare the bank reconciliation to the balance in the checkbook. Any differences should be reconciled. The Sheriff should document this by initialing the bank reconciliation and the balance in the checkbook.
- The Sheriff should approve all disbursements and sign all checks.

*Sheriff's Response: None*

INTERNAL CONTROL - MATERIAL WEAKNESSES:

None.

PRIOR YEAR:

The Sheriff Should Assure That The Fiscal Court Sets Salaries For His Office  
The Sheriff's Office Lacks Adequate Segregation Of Duties

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND  
ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF THE FINANCIAL  
STATEMENT PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

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The Honorable L.C. Reese, Lee County Judge/Executive  
Honorable Harvey Pelfrey, Lee County Sheriff  
Members of the Lee County Fiscal Court

Report On Internal Control Over Financial Reporting And  
On Compliance And Other Matters Based On An Audit Of The Financial  
Statement Performed In Accordance With Government Auditing Standards

We have audited the statement of revenues, expenditures, and excess fees - regulatory basis of the Lee County Sheriff for the year ended December 31, 2005, and have issued our report thereon dated August 4, 2006. The County Sheriff's financial statement is prepared in accordance with a basis of accounting other than generally accepted accounting principles. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Lee County Sheriff's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statement and not to provide an opinion on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statement. The reportable condition is described in the accompanying comments and recommendations.

- The Sheriff's Office Lacks Adequate Segregation Of Duties

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statement being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable condition described above is not a material weakness.

Report On Internal Control Over Financial Reporting And  
On Compliance And Other Matters Based On An Audit Of The Financial  
Statement Performed In Accordance With Government Auditing Standards  
(Continued)

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the Lee County Sheriff's financial statement for the year ended December 31, 2005, is free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the accompanying comments and recommendations.

- The Sheriff Should Require The Depository Institution To Pledge Or Provide Sufficient Collateral And Enter Into A Written Agreement To Protect Deposits
- The Fiscal Court Should Set The Deputies And Assistants Salary Limit

This report is intended solely for the information and use of management and the Kentucky Governor's Office for Local Development, and is not intended to be and should not be used by anyone other than the specified parties.

Respectfully submitted,

  
Morgan-Franklin, LLC

Audit fieldwork completed -  
August 4, 2006